

UNITED STATES BANKRUPTCY COURT
NORTHERN DISTRICT OF CALIFORNIA

In re No. 02-40844 J
Chapter 11

SMITH BROS. MOTORS, INC. dba
SMITH, SMITH CHRYSLER, SMITH
DODGE, and SMITH JEEP,

Debtor.

DECISION - BANK ONE'S MOTION FOR
LEAVE AND STANDING TO INITIATE SURCHARGE ACTION

Creditor Bank One, N.A. ("Bank One") has moved the court for an order granting it leave and standing to pursue a surcharge action under Bankruptcy Code § 506(c)¹ against Amresco Commercial Finance, Inc. ("Amresco"). The motion is opposed by Amresco and by David A.

¹ Bankruptcy Code § 506(c) provides: "The trustee may recover from property securing an allowed secured claim the reasonable, necessary costs and expenses of preserving, or disposing of, such property to the extent of any benefit to the holder of such claim."

All further section references herein are to the Bankruptcy Code, 11 U.S.C. § 101 et. seq.

1 Bradlow, chapter 11 trustee herein (the "trustee"). The court holds
2 that even if it has the authority to permit Bank One to assert
3 derivatively the trustee's standing under § 506(c), the facts here
4 do not justify the granting of such relief. The court will
5 therefore deny Bank One's motion.

6 A. Background

7 The relevant facts are essentially undisputed. The debtor,
8 which operates a new and used car dealership, filed a voluntary
9 chapter 11 petition herein on February 15, 2002. On March 28, 2002,
10 the court appointed the trustee to serve as representative of the
11 debtor's estate.

12 At the date of the petition, Bank One and Amresco were holders
13 of security interests in the debtor's property. Bank One claims a
14 first priority lien as to the debtor's new and used motor vehicles
15 and the proceeds thereof; Amresco claims a first priority lien on
16 the debtor's accounts receivable (other than those arising from the
17 sale of a motor vehicle), equipment, and franchise rights. Pursuant
18 to an Intercreditor Agreement that Richard Smith, the debtor's
19 principal, executed in his individual capacity after the filing of
20 the petition, Bank One also claims a lien on 58% of Richard Smith's
21 personal assets, and Amresco claims a lien on the remaining 42%.
22 The parties do not concede, and the court has made no finding as to,
23 the relative priorities of Bank One and Amresco in any assets of the
24 debtor or Richard Smith.

25 Shortly after the filing of the petition, the debtor needed to
26 use the "cash collateral," as defined in § 363(a), of Bank One and

1 Amresco to operate its business, and entered into a stipulation with
2 them by which Bank One and Amresco permitted the debtor to use their
3 cash collateral pursuant to the provisions thereof. The court
4 approved the stipulation pursuant to several interim orders and a
5 final order, which was entered March 7, 2002.

6 After the appointment of the trustee, the trustee found the
7 estate in need of additional financing to fund the debtor's
8 business, and negotiated a loan with Amresco that would provide the
9 estate with additional financing of up to \$2 million. The court
10 approved the financing arrangement pursuant to an interim order and
11 a final order, which was entered on May 20, 2002. Bank One did not
12 object to entry of the order, participated in the negotiation of its
13 terms, and approved the form and content thereof.

14 Thereafter, a dispute between Amresco and Bank One surfaced as
15 to which creditor had the superior lien claim to certain valuable
16 franchise rights of the debtor's Chrysler dealership. Amresco
17 contends that as of the petition date, the franchise rights belonged
18 to the debtor, and thus, are subject to its prepetition security
19 agreement with priority over any conflicting security interest of
20 Bank One. Bank One contends that the franchise rights belong to
21 Richard Smith, individually, and thus, that it has a pro rata 58%
22 interest in such franchise rights pursuant to the above-mentioned
23 Intercreditor Agreement.

24 Apparently fearful that Amresco's claim to the franchise rights
25 might prove to be superior to its own, Bank One filed the present
26 motion. Bank One contends that the estate is unable to compensate

1 it for the cash collateral that the estate consumed, and that its
2 "superpriority" administrative claim under Bankruptcy Code § 507(b)²
3 will prove to be worthless because of all the liens on estate
4 property. Bank One further contends that it consented to the use of
5 its cash collateral and to the financing by Amresco on the
6 assumption that it had a valid lien on 58% of the franchise rights,
7 and that it "would never have consented . . . had it not firmly
8 believed that it would receive a 58% allocated share of the sales
9 proceeds of the Franchise Rights." Motion, pages 6-7. Bank One
10 also argues that at the time it provided the foregoing consents, it
11 believed that its "replacement lien rights and 'superpriority'
12 administrative expense claim . . . due to the estate's use of its
13 cash collateral would have little or no value" and that "the only
14 reason [it] perceived that it should proceed . . . at that time was
15 to garner the value of the Franchise Rights upon a sale of the
16 Dealership." Motion, page 7.

17 Bank One therefore now asks for the court's authority to pursue
18 a surcharge action against Amresco seeking to surcharge Amresco's
19 collateral in an amount equal to the greater of Bank One's loss
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21 ²Section 507(b) provides, in relevant part: "If the trustee,
22 under section . . . 363 . . . of this title, provides adequate
23 protection of the interest of a holder of a claim secured by a
24 lien on property of the debtor and if, notwithstanding such
25 protection, such creditor has a claim allowable under subsection
26 (a)(1) of this section arising from . . . the use, sale, or lease
of such property under section 363 of this title, . . ., then
such creditor's claim under such subsection shall have priority
over every other claim under such subsection."

1 resulting from its post-petition financial accommodations to the
2 estate, or 58% of the value of the franchise rights at issue.
3 Motion, page 13.

4 B. Discussion

5 Bank One concedes that, absent leave of court, it lacks
6 standing to prosecute an action under § 506(c). In Hartfort
7 Underwriters Ins. Co. v. Union Planters Bank, N.A., 530 U.S. 1, 120
8 S. Ct. 1942 (2000), the Supreme Court held that because § 506(c)
9 vests the right to seek a surcharge of a secured party's collateral
10 exclusively in "the trustee," a party other than the trustee has no
11 independent right to seek a surcharge under § 506(c). Id. at 1951.
12 The Supreme Court, however, expressly left open the question whether
13 a bankruptcy court could "allow other interested parties to act in
14 the trustee's stead in pursuing recovery under § 506(c)." Id. n.5.
15 Not surprisingly, Bank One requests the court to answer this
16 question in the affirmative, and Amresco and the trustee ask the
17 court to answer in the negative.

18 Prior to Hartford Underwriters, it had been well established in
19 the Ninth Circuit that a bankruptcy court may, in appropriate
20 circumstances, confer derivative standing on an official committee
21 of creditors to prosecute avoidance actions under Bankruptcy Code §§
22 547, 548, and 549 on behalf of the trustee. See, e.g., In re
23 Parmatex, Inc., 199 F.3d 1029 (9th Cir. 1999). In Parmatex, the
24 court stated that such granting of derivative standing was
25 appropriate when the trustee stipulated that the creditor's
26 committee could sue on his behalf, and the court approved the

1 stipulation. Id. at 1031. See also In re Spaulding Composites Co.,
2 Inc., 207 B.R. 899 (9th Cir. BAP 1997).

3 After Hartford Underwriters, the Second Circuit held that a
4 creditor could assert fraudulent transfer claims vested in the
5 trustee under § 548(a), if: (a) the trustee consents, and (b) the
6 court finds that the action is in the best interest of the estate
7 and is necessary and beneficial to the efficient resolution of the
8 bankruptcy proceedings. In re Housecraft Industries USA, Inc., 310
9 F.3d 64, 70 (2d Cir. 2002).³

10 Even if a court may, notwithstanding Hartford Underwriters,
11 authorize a party other than the trustee to act on the trustee's
12 behalf in asserting an avoidance action under § 547, 548, or 549, it
13 does not automatically follow that the court may authorize a party
14 other than the trustee to bring an action under § 506(c). This is
15 so because the proceeds of a recovery under § 547, 548, or 549 will
16 generally go to and benefit the estate, whereas a recovery under
17 § 506(c) by a party other than the trustee would pass "directly to
18 the claimant with no gain to the estate." In re Debbie Reynolds
19 Hotel & Casino, Inc., 255 F.3d 1061, 1067 (9th Cir. 2001) quoting In
20 re Palomar Truck Corp., 951 F.2d 229, 232 (9th Cir. 1991) (Although
21 Palomar's holding as to standing under § 506(c) was overruled by
22 Hartford Underwriters, the court in Debbie Reynolds stated that the
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24 ³In In re Cybergenics Corp., 304 F.3d 316 (3d Cir. 2002),
25 the Third Circuit initially reached the opposite conclusion. On
26 November 18, 2002, however, the court vacated its opinion to
permit a rehearing en banc.

1 above-quoted language in Palomar survived Hartford Underwriters).
2 Thus, the considerations concerning derivative standing under
3 §§ 547, 548, and 549, on the one hand, and under § 506(c), on the
4 other, are not the same.

5 The court's attention has not been directed to any cases
6 decided after Hartford Underwriters where a court authorized a party
7 other than the trustee to assert the trustee's rights under
8 § 506(c).⁴

9 Here, the court need not resolve the issue of whether it may,
10 in an appropriate case, confer derivative standing on a party to
11 assert the trustee's rights under § 506(c). This is so because even
12 if the answer is in the affirmative, this is not an appropriate case
13 for the court to do so.

14 The trustee has not consented to allow Bank One to act in his
15 stead, a factor that has been held to be determinative, at least
16 when the trustee is not acting unreasonably. See Parmatex, 199 F.3d
17 at 1031; Housecraft Industries, 310 F.3d at 70.

18 Nor is the trustee acting unreasonably, or in violation of his
19 fiduciary duty. As the trustee persuasively argues, during his
20 tenure, the court authorized the trustee to use a stipulated amount
21 of Amresco's cash collateral in accordance with a stipulated budget,
22 and to borrow funds from Amresco, on stipulated terms. In each
23 case, Bank One and all other parties were notified of the proposed

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25 ⁴In In re Suntastic USA, Inc., 269 B.R. 846 (Bankr. D. Ariz.
26 2001), the court concluded that it had no authority to confer
standing under § 506(c) to a party other than the trustee.

1 terms, and did not object. In each case, the stipulations were
2 approved by the court. It was never contemplated by the trustee, or
3 Amresco, that in addition to the stipulated financial concessions it
4 made to preserve the going concern value of the estate, Amresco
5 would also be subject to an involuntary surcharge by the trustee to
6 cover any losses beyond those that might have resulted from the
7 expenditures contemplated by the stipulated budgets. That simply
8 was not the deal the parties made.

9 For the foregoing reasons, the trustee acknowledges, not
10 unreasonably, that he does not have a valid surcharge claim against
11 Amresco under § 506(c). Bank One, standing in the shoes of the
12 trustee, can fare no better.

13 Nor is there any allegation that either the trustee or Amresco
14 breached the cash collateral and financing stipulations or violated
15 the orders approving same. Indeed, Bank One does not dispute that
16 the trustee did not exceed the agreed upon budgets, and that Amresco
17 complied with its end of its bargain with the trustee.

18 Bank One's main argument, rather, is that its expectation of
19 having a 58% interest in the debtor's franchise rights may be
20 disappointed, and that "equity" dictates that it be allowed to
21 surcharge Amresco's collateral to make up for any such
22 disappointment. This argument fails for numerous reasons.

23 First, there is no allegation that Amresco engaged in any
24 misconduct or misrepresentations that victimized the trustee. The
25 trustee was not even a party to the Intercreditor agreement under
26 which Bank One claims its 58% interest in the franchise rights.

1 Therefore, whatever disappointments or wrongs that Bank One believes
2 resulted from the Intercreditor Agreement did not vest any surcharge
3 rights in the trustee. Again, Bank One standing in the shoes of the
4 trustee can fare no better.

5 Second, the purpose of § 506(c) is to compensate the estate
6 when it expends funds to protect and preserve the collateral of a
7 secured party. See In re Cascade Hydraulics and Utility Service,
8 Inc., 815 F.2d 546, 548 (9th Cir. 1987). Thus, its purpose is not
9 to compensate a secured party who miscalculated the value or
10 priority of its lien position, even if the party made financial
11 concessions to the estate as a result of the miscalculation. Id.
12 See also Debbie Reynolds, 255 F.3d at 1068.

13 The fact that Bank One's motion is outside the perimeter of
14 § 506(c) is underscored by the relief Bank One states it will seek
15 from Amresco if the motion is granted: a surcharge in an amount
16 equal to the greater of Bank One's loss resulting from the post-
17 petition financial accommodations to the estate it agreed to,
18 allegedly in reliance on it having a 58% interest in the franchise
19 rights, or 58% of the value of the franchise rights at issue.
20 Motion, page 13. Clearly, neither measure is an appropriate remedy
21 under § 506(c), or in keeping with its purpose. Rather, a surcharge
22 is appropriate only when a "concrete" and "quantifiable" benefit has
23 been conferred on the secured party to be surcharged, see In re
24 Compton Impressions, LTD., 217 F.3d 1256, 1261 (9th Cir. 2000);
25 Debbie Reynolds, 255 F.3d at 1068, and the appropriate amount of the
26 surcharge is the amount expended "directly to protect and preserve

1 the collateral" of the secured party. Casecade Hydraulics, 815 F.2d
2 at 548.

3 In the present context, Bank One's disappointed expectations as
4 to the franchise rights, although unfortunate from Bank One's
5 standpoint, are simply irrelevant. The facts here confer no
6 § 506(c) rights on the trustee, or derivatively, on Bank One. Nor
7 do they justify imposition of a surcharge against Amresco's
8 collateral.

9 C. Conclusion

10 For the foregoing reasons, the court will issue its order
11 denying Bank One's motion.

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13 Dated: December 5, 2002
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Edward D. Jellen
United States Bankruptcy Judge
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